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SUBJECT: ROMANIA: PRIVATIZATIONS PROGRESSES, BUT MORE WORK
AHEAD

REF: A) BUCHAREST 02153, B) BUCHAREST 03902, C) BUCHAREST

02058

SUMMARY

1. Romania made substantial progress in privatizing state-owned assets in 2004, a year which could be dubbed "the year of energy privatizations." Major priorities for 2005 include completion of energy privatizations, privatization of the Romanian Commercial Bank and National Savings House, and attaching tax arrears run up by state-owned and favored private companies. END SUMMARY

2004 - Decisive Year for Energy Sector Privatizations

2. The completion of privatizations is necessary for Romania to become a fully functioning market economy. The sale of a 25% stake in Romania's largest commercial bank to the European Bank for Reconstruction and Development (EBRD) and International Finance Corporation (IFC) for \$222 million as well as privatizations of the giant oil company Petrom and four major energy distributors contributed significantly to Romania's \$4.4 billion FDI inflow in 2004.

3. In transactions totaling an estimated \$3 billion, five privatizations in the energy sector resulted in European investors taking control of key companies forming the backbone of the Romanian energy sector. Austrian group OMV paid \$2 billion for the former state-owned petroleum corporation Petrom. Before taking over Petrom, OMV was a secondary player in the oil market. After acquiring Petrom, however, OMV's market share rose from 6% to 30% in Romania and to an estimated 18% in the Danube region. The Italian group ENEL paid \$147 million for the electric distribution companies Electrica Banat and Electrica Dobrogea. The GOR signed a privatization contract for the sale of 30% of Distrigaz Nord on October 2004 with the German firm Ruhrgas for \$165 million, with a further investment of \$236 million forthcoming to ensure Ruhrgas's equity share reaches 51%. In the same month, Gaz de France signed an agreement to take over Distrigaz Sud in a transaction worth approximately \$410 million. These two privatizations will be finalized in 2005.

Which Privatization Authority?

4. While the Authority for State Asset Resolution (AVAS), which was formed last March through the merger of the Authority for Banking Asset Resolution and the Authority for Privatization and Management of State Shareholding (APAPS) is generally referred to as the "privatization authority," it is not the only entity involved in the privatization of state assets. Equally important is the Office for State Shareholding and Privatization in Industry (OPSPI) under the Ministry of Economy and Commerce, which controls privatizations in the energy production and mining sectors. Other ministries also control state assets. The most notable is the Ministry of Public Finances, which is in charge of the sale of The National Savings Bank (CEC). Under Romanian practice, privatization decision-making and negotiations are conducted with the privatization entity which owns the asset. Moreover, major privatizations such as those in the energy or banking sector, or divestiture of socially sensitive industrial plants must be approved by the cabinet and the Parliament.

2005 Privatization Plan

5. In the energy sector, the focus will be on:
-- Electric Power Distribution. Complete the privatization of Electrica Moldova with E.ON (Germany) and of Electrica Oltenia with CEZ (Czech Republic); proceed with the privatization of Electrica Muntenia Sud, which supplies electricity for the area including Bucharest (PriceWaterhouseCoopers is the privatization consultant); and initiate privatization of three remaining branches (Electrica Transylvania Nord, Electrica Transilvania Sud, and Electrica Muntenia Nord).
-- Electric Power Generation. The OPSPI is preparing for

sale three coal and gas-based integrated energy complexes (Turcenii, Rovinari and Craiova). Deloitte Central Europe has been selected as the privatization consultant.

16. In the banking sector, AVAS's priority is the privatization of the Romanian Commercial Bank (BCR) one of the commitments undertaken in the GOR's agreement with the IMF. Highly respected names in international finance, including the German group HVB, Deutsche Bank, Unicredito and Erste Bank have indicated an interest in BCR, the largest Romanian bank in terms of assets. The Ministry of Public Finance plans to initiate the privatization of the National Savings Bank (CEC) this year. CEC is the largest credit institution in Romania in terms of the number of branches.

17. In the industrial sector, AVAS sold 62 medium and large companies in which the state was a majority shareholder in 2004. In addition to these transactions, AVAS privatized minority stakes in 85 companies, resulting in revenues to the state of approximately \$381.2 million. AVAS still holds stock in some 1,000 companies, although half of these are non-privatizable, most of them subject to liquidation. Of the remaining 500 companies, AVAS has majority stakes in only approximately 100. One of these is Electroputere, an electric motor manufacturer located in Craiova. After repeated failures to privatize the company as an integrated whole, AVAS plans to re-launch the privatization process, splitting up the company into units to make it more attractive to investors. Success will depend upon how the units are packaged, as only the locomotive production unit and the rotating electric machine unit have attracted investor interest.

Mind the Devil in the Details

18. Investors are cautioned to exercise due diligence in privatizations, to undertake their own thorough independent investigation, and not to rely primarily on the information and representations found in privatization documents. Having a good local counsel with solid knowledge of the intricate Romanian privatization process and state aid legislation is crucial to success. Buyers of state-owned companies must negotiate requirements and restrictions concerning the company's purpose, scope of activities, turnover, and social protections in the form of limited layoffs or funding for retraining programs. Privatizing agencies continue the practice of rolling into privatization agreements provisions of previously negotiated collective labor agreements, which are labor-protective and restrict layoffs.

Comment

19. Prime Minister Tariceanu has implied AVAS and OPSPI will merge into one agency in summer 2005. Post will continue to work with the GOR privatization agencies, advocating for transparency in the privatization process and fair treatment of investors. End Comment.

10. AmEmbassy Bucharest's reporting telegrams are available on the Bucharest SIPRNet website:
www.state.sgov.gov/p/eur/Bucharest/.

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